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**USTR Mickey Kantor Orders 100% Tariffs
on More Than \$1 Billion of Chinese Imports
Cites China's Failure to Protect U.S. Intellectual Property**

Ambassador Mickey Kantor today ordered the imposition of 100% tariffs on \$1.08 billion of imports of Chinese products into the United States because of China's failure to protect and enforce the intellectual property rights (IPR) of U.S. companies and to provide market access for intellectual property-based products and industries.

From 1984 through 1994, U.S. yearly exports to China rose from \$3 billion to \$8.8 billion. In the same period, however, Chinese exports to the U.S. rose from \$3.1 billion to almost \$38 billion. The bilateral trade relationship is seriously imbalanced. The United States is the world's largest open economy, while that of China remains closed to many of our most competitive export sectors.

China's failure to enforce the intellectual property rights of U.S. companies and its persistent denial of market access for intellectual property-based products and industries has damaged U.S. commerce and caused serious losses to American companies and workers.

"We cannot stand by while the interests of our fastest growing, most competitive industries are sacrificed in China. I have said that we would take action by reducing China's access to the U.S. market if China does not protect our computer software, pharmaceuticals, agricultural and chemical products, audiovisual works, books and periodicals, and trademarks. Today's action represents the largest retaliation ever taken by the U. S. government," Kantor said. "So far, the Chinese have taken some steps, but they have not addressed the major substantive problems — or the continuing operation of Chinese factories that mass-produce pirated products for export."

"This morning I met with Ambassador Li Daoyu of China to inform him that the United States was taking this action. I indicated that the U. S. stands ready to engage in serious negotiation, but that these trade sanctions will automatically become effective if no acceptable agreement is reached by February 26."

Background

USTR Kantor's announcement is the result of an eight-month investigation under the Special 301 provision of the Trade Act of 1974 into China's intellectual property rights enforcement practices. Under the statute, the investigation, which was initiated on June 30, 1994, can run up to six months, with the possibility of a 90 day extension. On December 31, USTR Kantor issued a proposed determination that China's IPR enforcement practices are unreasonable and burden or restrict U. S. commerce, and USTR published a proposed retaliation list of \$2.8 billion. At the same time, Kantor extended the investigation until February 4 to allow negotiators time to pursue an acceptable settlement.

Nine days of negotiations on IPR enforcement held in Beijing concluded on January 28 without agreement. Although some progress was made during these negotiations, China failed to make the commitments necessary to permit resolution of the Special 301 investigation.

While China has made significant improvements in its IPR legal regime as a result of the 1992 U.S.-China Memorandum of Understanding on Intellectual Property Protection, piracy of copyrighted works and trademarks is rampant in China.

Piracy of computer software -- one of the most competitive industries of the United States -- runs as high as 94%, according to U.S. software industries. Chinese piracy of U.S. CDs, laser discs, cassette tapes, books, video games, videos and movies is close to 100% in many parts of China.

In the past two years, Chinese companies have begun to export pirated products in large volume -- despoiling markets in southeast Asia and even reaching Latin America, Canada, and the United States. This trend is exemplified by the fact that 29 CD and LD factories in China have a production capacity of 75 million CDs for a domestic market that can absorb only 5 million CDs annually. In addition, some of these factories have begun to produce and export CD-ROMS, which can hold dozens of computer software programs and other copyrighted works on a single disk. To date, despite repeated U.S. requests, China has taken no significant action to stop infringing activities in these factories.

The Chinese Products Subject to Retaliation

The final list, which will appear shortly in the Federal Register, is comprised of 35 product categories of high-growth Chinese exports to the United States. Among the principal products included on the list are: answering machines and cellular telephones; a wide variety of plastic articles; and sporting goods, such as fishing rods, gymnastic equipment and surf boards.

The final list was selected from a broad preliminary list of product categories from China's key export industries. It was created subject to specific criteria designed to minimize any impact on U.S. industry, workers and consumers.

The tariffs will be imposed automatically by the U. S. Customs Department on February 26, 1995 -- thereby allowing several weeks for goods that are in transit to enter the United States before the duties are imposed.

China IPR FACT SHEET

Special 301 Investigation

On February 4, 1995, U.S. Trade Representative Kantor ordered the imposition of 100 % tariffs on \$1.08 billion of imports of Chinese products into the United States because of China's failure to protect and enforce the intellectual property rights (IPR) of U.S. companies and to provide market access for intellectual property-based products.

China's failure to enforce the intellectual property rights of U.S. companies and its persistent denial of market access for intellectual property-based products has damaged U.S. commerce and caused serious losses to American companies and workers.

The tariff increases will go into effect on February 26, providing sufficient time for goods that have left Chinese ports as of February 4 to clear U.S. Customs before the new duties go into effect.

On February 4, Ambassador Kantor met with China's Ambassador Li Daoyu to inform him of the action the United States was taking. In addition, Kantor extended an invitation to China to resume negotiations.

Ambassador Kantor identified China as a Priority Foreign Country under the 1974 Trade Act on June 30, 1994, and immediately initiated a Special 301 investigation into China's intellectual property rights (IPR) enforcement practices. Under the statute, the investigation runs for up to six months, with a possible three-month extension. At the end of the six month investigation, in this instance December 30, 1994, the USTR made a proposed determination that China's IPR enforcement practices are unreasonable and burden or restrict U.S. commerce. In addition, Kantor authorized publication of a proposed list of Chinese products to which tariffs of 100% could be attached. That list was valued at \$2.8 billion. Ambassador Kantor extended the investigation until February 4, 1995, as a result of the complexity of the negotiations.

The List

The final list, which will appear shortly in the Federal Register, is comprised of 35 product categories of high-growth Chinese exports to the United States and includes items in which the Chinese Government has substantial involvement, such as silk products and bicycles. The top five categories of items on the retaliation list are:

**U.S. Imports
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1.	Miscellaneous plastic articles (e.g. picture frames, baseball card holders, etc.)	\$465 million
2.	Answering machines & cellular telephones	\$108 million
3.	Sporting goods (e.g., fishing rods, gymnastics equipment & surf boards)	\$78 million
4.	Wooden articles (e.g. picture frames, ornaments, jewelry boxes)	\$70 million
5.	Bicycles (with wheels 20" & smaller)	\$65 million

Other articles on the list include: candies; mushrooms; citric acid; rubber gloves; leather trunks and containers; greeting cards; silk gloves, handkerchiefs and scarves; gold and platinum jewelry; kitchen ware, and copper articles, metal furniture and counters, and non-electric lamp fittings.

The final list was developed after reviewing more than 190 written submissions and testimony presented by the public during two days of hearings and a thirty-day comment period. The hearings addressed the impact the inclusion of particular products on the final list would have on U.S. industries and consumers. U.S. government agencies selected products that would have a clear impact on China, but would cause minimal harm to the U.S. economy, its businesses and workers. For example, the list minimizes, to the extent possible, a disproportionate adverse impact on small and medium-size firms and generally avoids items for which there is no U.S. production or alternate foreign suppliers.

The size of the list is based on the estimates of U.S. government economists on the damage done to the U.S. economy by China's failure to protect effectively intellectual property rights — that is, losses suffered in China due to Chinese infringement of U.S. copyrighted works, trademarks, and patented products. In addition, we are setting up an interagency group to determine the damage done to the United States by exports to third countries.

U.S.-China Trade Relations

U.S.-China bilateral trade has grown significantly since relations were normalized in 1979, with two-way trade approaching \$50 billion in 1994 compared with \$2.3 billion in 1979. At the same time, the bilateral trade relationship has become badly imbalanced, with the U.S.

trade deficit with China skyrocketing from \$70 million in 1983 to almost \$30 billion in 1994. China's imports to the United States during that period have risen 929% (rising from \$3.1 billion to almost \$38 billion in 1994) while U.S. exports to China have gone from \$3 billion to almost \$9 billion during the same period.

Piracy in China

Overall, China has markedly improved its IPR legal regime as required by the 1992 U.S.-China Memorandum of Understanding on Intellectual Property Rights. China has not, however, lived up to its obligation under the Agreement to enforce its laws and regulations. Until recently, enforcement of intellectual property rights has been virtually absent, with piracy rates soaring in all major urban centers along China's increasingly prosperous east coast.

IPR piracy in China is rampant. U.S. industries estimate that piracy of computer software and other copyrighted works rose sharply over the past year. Among the largest and most obvious offenders in China are the operators of 29 CD factories where U.S. copyrighted CDs, laser discs, and CD-ROMs are produced. These factories are largely in south and central China. With an annual production capacity exceeding 75 million CDs in a domestic market that has a capacity of 5 million, most of those pirated CDs, LDs, and CD-ROMs are destined for export, and pirated products are now found in Hong Kong, southeast Asia, and increasingly, in the Americas.

Piracy of other audiovisual works, particularly audiocassettes, videos and video games in China, runs close to 100% -- with little evidence of effective controls on this piracy to date. Piracy of other cutting-edge U.S. copyrighted products, particularly computer software, runs at about 94% -- and 100% in CD-ROMs, where no major U.S. computer software manufacturer has issued licenses for legal production in China. The administrative apparatus in China for policing copyright piracy is extremely weak. The National Copyright Administration offices are located in fewer than half of China's provinces, and have few qualified personnel and no real authority to take effective action against offenders. The courts, which do have real authority, have yet to issue substantial judgments in civil cases against Chinese defendants. To date, there have been no criminal convictions for major copyright infringers.

Piracy of trademarks is also rampant, especially in south China. Enforcement, while effective in some locales, is sporadic at best. China currently fails to protect well-known marks or to offer adequate and effective protection for service marks and other U.S. trademarks.

Negotiations

Negotiations with China have been underway for 20 months, including eight months under the Special 301 investigation. The President, members of the Cabinet, and very senior U.S. government officials have expressed concern at the highest levels of the Chinese government about the prevalence of piracy and the damage it causes U.S. economic interests. Since July of 1993 we have met with Chinese negotiators 21 times, including eight rounds in 1994 – five since the Special 301 investigation was initiated. A nine-day round of negotiations on IPR enforcement concluded on January 28 without agreement.

While agreement has not yet been reached, the Chinese have begun to take action – both on the ground and in terms of preliminary commitments that will improve IPR enforcement over time. In particular, China has launched a special enforcement period and has begun systematic raids in some regions against retailers, closing shops and levying tough fines. China has yet to take action, however, against manufacturers, including those involved in CD production.

What is Intellectual Property?

Intellectual property refers to a broad collection of rights relating to the products of human inventiveness and creativity. It comprises two main branches: first, industrial property, covering inventions, trademarks, and industrial designs; and, second, copyright.

Patent. A patent is a governmental grant of a property right to the inventor of a product or process which is new and has utility – that is, it has industrial application. A patent provides the inventor, or the inventor's successor in title, the exclusive right to the invention for a limited period of time. This right generally enables the patentee to exclude others from making, using or selling the invention. As a consequence, the patentee can also grant licenses to third parties, letting them exploit the invention on such terms as the patent may prescribe. The Uruguay Round TRIPS agreement requires that a patent must be valid for a minimum of 20 years from the filing date of the application. The patent term in the U.S. is 20 years from filing.

Trademark. A trademark is any word, symbol, design or device used to identify a product. Service marks involve similar descriptors to identify a service. The purpose of a trademark or service mark is to identify goods put on the market, thereby distinguishing them from other goods and services, and to indicate their source or origin. These marks enable consumers to recognize products they have previously purchased so that they can exercise their preference purchase them again. Accordingly, trademark owners usually make every effort to maintain or improve the quality of their goods. To a large extent, therefore, trademarks have become a guarantee of quality.

Protection of a trademark means that no person or enterprise other than its owner may use it — or any other trademark so similar to it that its use would lead to confusion in the minds of the public. The Trips agreement, for example, provides that initial registration of a trademark must be valid for a period of at least seven years, and that registration is renewable indefinitely.

Copyright. Copyright usually refers to "literary and artistic works". U.S. copyright law enumerates eight broad categories of protectible subject matter: literary works (which include computer software), musical works, including accompanying words, dramatic works, including accompanying music, pantomimes and choreographic works, pictorial, graphic and sculptural works, motion pictures and other audiovisual works, sound recordings and architectural works. Works that do not fall into these categories may be protected as well.

Copyright protection means that certain uses of a work are lawful only if made with the authorization of the owner of the copyright. The owner of a right may generally transfer a right, or license certain uses of the work. U.S. copyright law grants the owner exclusive rights to reproduce a work, to prepare derivative works based on it (e.g., to base a film on a book or play), and to distribute copies to the public by sale or other transfer of ownership, or by rental, lease or lending, to perform the work publicly (with the exception of sound recordings), and to display certain categories of works publicly. U.S. law, consistent with the Berne Convention and the TRIPS agreement, protects a copyrighted work for the term of author's life, plus 50 years.

EXAMPLES OF THE HARM CAUSED U.S. WORKERS BY PIRACY IN CHINA

A vast array of American workers rely on legitimate exports for their livelihoods. Rampant piracy in China is displacing those exports, not only to China but to third country markets that are being inundated with pirated product from China. The result is fewer jobs for U.S. workers.

Any number of examples could be cited, but let's use one familiar to all of us -- the Whitney Houston CD, the soundtrack of "The Bodyguard". This CD has sold 28 million copies in markets around the world. (Recorded music is a \$31 billion dollar industry -- not counting all the ancillary industries it 'multiplies' through. Last year, industry sales in the United States topped \$10 billion, and sales in the rest of the world reached over \$21 billion).

The Whitney Houston CD was made in a plant in Huntsville, Alabama where hundreds of workers guided it from a single, studio recording to the product bought by 28 million consumers the world over. The factory in Huntsville includes sales and marketing employees, customer service reps, sound engineers working with technical specs and laser equipment, technicians operating machines that mold and punch the discs, technicians operating machines that apply polycarbonate linings, disc colorists, paint mixers and silkscreeners, graphic artists who make the insert cards, packers who put the discs into their plastic cases, boxers, loading dock operators, production coordinators, back office personnel. And this doesn't even touch on the pre-production and post-production stages in which U.S. workers - our musicians, writers, mixers, studio producers, technical advisors, wholesale and retail sales clerks, to name a few, made their contribution. These are real people, and real jobs.

The same story can be told time and time again when we look at the scope of piracy in China. Additional examples of how U.S. right holders -- and thus U.S. workers -- are being harmed in China include:

- * On a recent visit to the showroom of the Shenfei plant in Shenzhen on Hong Kong's border, U.S. industry representatives found copies of over 30 U.S. movies for sale, such as "Twins," "City Slickers II," "Robocop," "Die Hard," "Out of Africa," "Terminator II," "Gone With the Wind," "Fantasia," "Beverly Hills Cop," and "Amadeus." None of these had been authorized for production in China. The showroom staff bragged that the pirated copies were being exported to South Korea, Taiwan, Singapore, Malaysia and Thailand, and that they were looking for new export markets all the time.
- * Some of the pirated films now being copied onto laser discs or video cassettes in China have not yet been released in those formats in the United States. For example, "Jurassic

Park" and the "Lion King" became available in China on laser disc before they were released on video in the United States.

- * One can walk into a video store in Beijing and find copies of U.S. works for sale. An industry representative recently visited one store and found copies of "Above the Law," "Under Siege," the James Bond library of films, and the made-for-television movies "Queenie," "Capone," and "Fight for Life."
- * While piracy of U.S. films is rampant in China, China currently mandates that only 10 "quality films" may be imported. As a result, the movie "Terminator II" could not be legally imported into China but it was a blockbuster hit in China's thousands of "video cinemas" -- which ran the pirated video version of the film with great commercial success.
 - When given the opportunity, U.S. films that are imported legally do very well. The "Fugitive," imported as one of this year's 10 quality foreign films, was an overwhelming commercial success.
- * The illegal use of famous U.S. brand names is also rampant in China. A few of the many examples include:
 - Cornflakes have become known as "Kongalu Cornstrips" to Chinese consumers -- a bogus product whose trademark and packaging is identical to that of Kelloggs Cornflakes.
 - Delmonte canned products are better known in China as "Jialong" -- a flagrantly pirated version of the Delmonte trademark.
 - Sun Microsystems' trademark has been appropriated and used by a Mr. Sun, a small-scale computer manufacturer in South China who successfully markets his products by using the Sun Microsystems trademark.
 - Mineral water drinkers in China can enjoy "Pabst Blue Ribbon Water," and, when chilled by the cool night air, they can wear "Pabst Blue Ribbon" parkas, on sale in stands near the U.S. Embassy in Beijing and in the Beijing Airport.
- * The Business Software Alliance, an association of major U.S. software manufacturers, estimates that 94 percent of the Chinese market is comprised of pirated software.
- * Pirated copies of U.S. software packages are freely sold on the streets and in stores in China. For example, anyone can

walk into a store in Beijing and buy a pirated copy of Microsoft's popular Windows software package. The store simply copies it onto a few blank floppy discs while you wait for a tiny fraction of its retail price. In some places, you can even get pirated copies of the manuals on how to use the software.

- * There is a growing concern among the U.S. software industry that the production of CD-ROMs containing pirated copies of U.S. packages will explode in the near future. CD-ROMs produced in China and containing unauthorized copies of U.S. works are now flooding the Hong Kong market.
- * Chinese companies and government ministries also pirate software on a large scale for internal use. Ministries' budgets reportedly do not include monies for the purchase of software, even though software is widely used within the government.
- * China now has a production capacity of over 75 million CDs, LDs, and DC-ROMs with a domestic market of only 5 million. The vast majority of U.S. sound recordings, movies and software copied in this manner is illegal. As a result, not only is the Chinese market flooded with pirated products, the over-capacity is exported all over Asia and as far away as Canada and the United States.
- * The CDs produced in huge quantities contain some of the most famous U.S. artists. One cache of CDs recently found in Guangzhou contained the pirated songs of Whitney Houston, Billy Joel, Michael Jackson and Kenny G.
- * The proliferation of these pirated works in China and in third-country markets prevents U.S. right holders from marketing their legitimate product in those markets.